Petition

81-2082

No.

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In the Supreme Court of the United States

OCTOBER TERM, 1981

CHARLES A. BOWSHER, COMPTROLLER GENERAL OF THE UNITED STATES, AND UNITED STATES OF AMERICA, PETITIONERS

v.

SMITHKLINE CORPORATION

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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QUESTION PRESENTED

Whether, with respect to negotiated government contracts, the Comptroller General is authorized by law to examine the contractor's books and records pertaining to costs of research and development, advertising and promotion, distribution, and administration, where such costs, although not allocated by the contractor to particular products or calculated on a product basis in determining price, are defrayed by the contractor from commingled general revenues that include the government's payments under the contract.

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SMITHKLINE CORPORATION

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The Solicitor General, on behalf of the Comptroller General of the United States and the United States of America, petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Third Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. A, *infra*, 1a–28a) is reported at 668 F.2d 201. The opinion of the district court (App. C, *infra*, 30a–50a) is reported at 483 F. Supp. 712.

JURISDICTION

The judgment of the court of appeals (App. B, *infra*, 29a) was entered on December 28, 1981. On March 19, 1982, Justice Brennan extended the time for filing a petition for a writ of certiorari to and including May 10, 1982. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTORY PROVISIONS INVOLVED

1. 10 U.S.C. 2313(b) provides:

> Except as provided in subsection (c), each contract negotiated under this chapter shall provide that the Comptroller General and his representatives are entitled, until the expiration of three years after final payment, to examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to, the contract or subcontract.

2. 41 U.S.C. 254(c) provides:

> All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts. Under regulations to be prescribed by the Administrator, however, such clause may be omitted from contracts with foreign contractors or foreign subcontractors if the agency head determines, with the concurrence of the Comptroller General of the United States or his designee, that the omission will serve the best interests of the United States. However, the concurrence of the Comptroller General of the United States or his designee is not required for the omission of such clause—
>
> (1) where the contractor or subcontractor is a foreign government or agency thereof or is precluded by the laws of the country involved from making its books, documents, papers, or records available for examination; and

(2) where the agency head determines, after taking into account the price and availability of the property or services from United States sources, that the public interest would be best served by the omission of the clause.

If the clause is omitted based on a determination under clause (2) a written report shall be furnished to the Congress. The power of the agency head to make the determination specified in the preceding sentences shall not be delegable.

STATEMENT

1. In 1973 and 1974, respondent SmithKline Corporation ("SmithKline") entered into three contracts with the Defense Supply Agency of the Department of Defense and two contracts with the Veterans Administration for the sale of pharmaceutical products to the government. Each of the five contracts was a negotiated fixed-price contract in which the price was based on petitioner's published catalogue price for the particular product; the total price for the contracts was approximately $3.3 million (App. C, *infra*, 31a, 44a n.7; C.A. App. 47–51)[1]. As required by 10 U.S.C. 2313(b)[2] and 41 U.S.C. 254(c),[3] each of the contracts contained a standard access-to-records clause in which respondent agreed that the "Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of three years after final payment under this contract * * *, have access to and the right to examine any directly pertinent books, docu-

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[1] "C.A. App." refers to the joint appendix filed by the parties in the court of appeals.

[2] This provision is applicable to the Defense Supply Agency contracts.

[3] This provision is applicable to the Veterans Administration contracts.

ments, papers, and records of the Contractor involving transactions related to this contract" (App. C, *infra*, 32a–33a; C.A. App. 48–53).

In May 1972, the General Accounting Office began "a two-phase study of the economics and operations of the pharmaceutical industry" (App. C, *infra*, 36a). In the first phase of the study, respondent and five other pharmaceutical firms agreed to permit GAO officials to visit and inspect their facilities and operations. The companies declined, however, to participate in the second phase of the study, which was designed to enable GAO to examine "the salient economic and operational aspects of the drug industry" (*ibid.*). Because of the companies' failure to cooperate, GAO abandoned its plans for the second phase of the study and proposed "a more modest study" based on data to be obtained under the foregoing access-to-records provisions (*id.* at 37a).

In August 1974, the Comptroller General wrote to the six companies, including petitioner, to request access to designated records pursuant to the access-to-records provisions. The Comptroller General explained that the request was part of "a review of the procurement of drugs by agencies of the Federal Government, including the pricing of drugs and pharmaceuticals procured under negotiated contracts" (*id.* at 37a–38a). To that end, the Comptroller General sought to examine (*id.* at 38a):

> all books, documents, papers, and other records directly pertinent to the contracts, which include, but are not limited to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests.

2. Respondent refused to comply with the Comptroller General's request. Instead, on February 20, 1975, it commenced the present action in the United States District Court for the Eastern District of Pennsylvania seeking declaratory and injunctive relief to bar GAO from access to its records. The United States subsequently intervened as a defendant and filed a counterclaim to require petitioner to allow the requested inspection (App. C, *infra*, 30a–31a, 38a).

Following discovery, the district court on January 24, 1980, granted the government's motion for summary judgment and denied respondent's cross-motion (App. C, *infra*, 30a–50a). Contrary to SmithKline's contention that the Comptroller General's request had been prompted by the assertedly improper purpose of "seeking information concerning profits in the pharmaceutical industry for dissemination to Congress and the public" (*id.* at 39a), the court found, "[o]n the basis of uncontroverted depositions and affidavits filed by the parties in connection with the motions for summary judgment" (*id.* at 31a), "that GAO's purpose is to compare cost to price of drugs purchased under specified contracts to determine the adequacy of the protections afforded the government in the contract negotiation process" (*id.* at 41a). Relying on the legislative history of the access-to-records statutes and the decision in *Hewlett-Packard Co.* v. *United States*, 385 F.2d 1013 (9th Cir. 1967), cert. denied, 390 U.S. 988 (1968), the court also concluded that the statutes were intended to enable GAO "to determine whether * * * there have been 'improprieties and wastefulness in the negotiation of contracts,' or whether * * * the contractor's costs are 'out of line with the contract price'" (App. C, *infra*, 44a–45a). Accordingly, the court held that the Comptroller General's purpose "to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests" (*id.* at 45a)

was "a purpose authorized by the statutes" (*id.* at 46a).

In addition, in view of the plain meaning of the statutes and the *Hewlett-Packard* decision, the court rejected petitioner's argument that the access-to-records provisions were entirely inapplicable to negotiated fixed-price contracts in which, as here, the price was based on the contractor's catalogue price (App. C, *infra*, 44a n.7).

Finally, in accordance with *Hewlett-Packard* and *Eli Lilly & Co.* v. *Staats*, 574 F.2d 904 (7th Cir.), cert. denied, 439 U.S. 959 (1978), the court held that, at least with respect to the pharmaceutical industry, the access provisions are not limited to records of "the direct costs of manufacturing the drug covered by the contract" but include "the records of all costs which go into the make-up of the price of the drug covered in the contract" (App. C, *infra*, 47a). The court recognized that the direct-cost "limitation, in the drug industry, would defeat the purpose of the access-to-records statutes since, as the Court in *Eli Lilly* pointed out, manufacturing and distribution costs of drugs have been estimated to constitute as little as nine percent of the product's sale price" (*ibid.*). Construing the statutes "in light of their purpose to permit a determination as to whether costs are 'out of line with the contract price'" (*ibid.*, quoting *Hewlett-Packard Co.* v. *United States*, *supra*, 385 F.2d at 1016), the court "agree[d] with Eli Lilly's reasoning that 'the access-to-records clauses should be interpreted so that an item is "directly pertinent" to a contract if it is a significant input in the price of the product purchased in the contract'" (App. C, *infra*, 47a).

Pursuant to its opinion, the district court entered summary judgment for the government and ordered (App. C, *infra*, 48a):

> that the Comptroller General of the United States and his duly authorized representatives have the

> right to examine all books, documents, papers, or records directly relating to the pricing and cost of producing items furnished by [respondent] under the following contracts * * *, including, but not limited to, records of experienced costs, including costs of materials, labor, overhead, distribution, research and development, and marketing, and such other costs as are directly pertinent to the drugs covered in the enumerated contracts * * *.

The court's order also included "provisions concerning the confidentiality of records, as agreed by the parties" (*ibid.*).

3. Respondent appealed to the United States Court of Appeals for the Third Circuit. During the pendency of the appeal, this Court granted the government's petition for a writ of certiorari in *Staats* v. *Bristol Laboratories*, 451 U.S. 400 (1981). The court of appeals accordingly deferred decision in this case pending disposition of *Bristol Laboratories*.[4] On April 29, 1981, the Second Circuit's judgment in *Bristol Laboratories* was affirmed by an equally divided Court (Justice Stewart not participating).

Following this Court's action in *Bristol Laboratories*, the Third Circuit decided SmithKline's appeal. The court of appeals rejected respondent's contention that GAO's motives could defeat its access to records, noting that "no court has found that GAO is precluded from demanding records from pharmaceutical firms because of an improper purpose" (App. A, *infra*, 13a–14a). The court also rejected respondent's argument that the Comptroller General has no authority to request cost records for fixed-price contracts (*id.* at 16a). However, the court disagreed with the district court's definition

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[4] While the appeal in this case was pending in the court of appeals, SmithKline filed a conditional petition for a writ of certiorari before judgment. The petition was denied on December 8, 1980. 449 U.S. 1038.

of "directly pertinent" records; consequently, it restricted GAO's access to respondent's allocated costs in accordance with the standard formulated by the district court in *Bristol Laboratories* (*id.* at 24a). The court therefore concluded that (*id.* at 27a):

> SmithKline must allow GAO personnel to inspect its records with respect to manufacturing costs, manufacturing overhead, royalty expenses, and delivery costs. SmithKline need not produce data with respect to research and development, marketing and promotion, distribution and administration, except to the extent that these costs may be included in the manufacturing costs.

REASONS FOR GRANTING THE PETITION

The question presented for review in this case, concerning the Comptroller General's right of access to records of government contractors, is identical to that presented in the government's petition in *Bowsher* v. *Merck & Co.*, cert. granted, No. 81–1273 (Apr. 19, 1982). Accordingly, this petition should be held pending the disposition of that case.

CONCLUSION

The petition for a writ of certiorari should be held pending the decision in *Bowsher* v. *Merck & Co.*, No. 81–1273, and should then be disposed of as appropriate in light of that decision.

Respectfully submitted.

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MAY 1982

APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

No. 80-1464

SMITHKLINE CORPORATION,
Appellant

v.

ELMER STAATS, Comptroller General
of the United States, and
THE UNITED STATES OF AMERICA,
Appellees

APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Argued July 16, 1981

Before: SEITZ, *Chief Judge*,
VAN DUSEN and HIGGINBOTHAM, *Circuit Judges*

(Filed December 28, 1981)

OPINION OF THE COURT

SEITZ, *Chief Judge.*

SmithKline Corporation appeals from a final judgment of the district court granting the Government's motion for summary judgment and holding that the Comptroller General (the Comptroller) has the right of access to records of costs "of materials, labor, overhead, distribution, research and development and marketing, and such other costs as are directly pertinent to the drugs purchased" under several contracts between the United States and SmithKline. *SmithKline Corp. v. Staats*, 483 F. Supp. 712, 722 (E.D. Pa.), *conditional petition for cert. before judgment denied*, 449 U.S. 1038 (1980). This court has jurisdiction under 28 U.S.C. §1291 (1976).

I.

During 1973 and 1974, SmithKline entered into five negotiated contracts[1] to supply drugs to the Veterans Administration and the Defense Supply Agency. As required by statute, each contract contained an access-to-records provision granting the Comptroller access to "any directly pertinent" records "involving transactions related to this contract." *See* 10 U.S.C. §2313(b) (1976) (Defense Supply Agency); 41 U.S.C. §254(c) (1976) (Veterans Administration).

In 1971, Senator Gaylord Nelson, chairman of a subcommittee investigating the pharmaceutical industry, learned of the access-to-records provisions contained in certain government contracts and urged that the General Accounting Office (GAO) invoke the provisions: "I think that we ought to take a look at some of those costs." *Competitive Problems in the Drug Industry: Hearings on Present Status of Competition in the Pharmaceutical Industry Before the Subcomm. on Monopoly of the Senate Select Comm. on Small Business*, 91st Cong., 2d Sess. 8020 (1971). One of Senator Nelson's staff assistants, Ben Gordon, explicitly stated that specific cost and price data should be secured by individual company and product, and that "such data should be made public." Gordon demanded on behalf of Senator Nelson that the data be sought "through the courts if necessary," and "without any strings attached so that the information could be used as needed." Similarly, a

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1. In negotiated procurements, the Government discusses the terms of the procurement with one or more contractors, with the contract going to the candidate whose proposal is most advantageous to the Government. Negotiated contracts are to be distinguished from advertised procurements, which award contracts on the basis of competitive bids submitted by contractors. *See* Case Comment, *The Comptroller General's Authority to Examine the Private Business Records of Government Contractors:* Eli Lilly & Co. v. Staats, 92 Harv. L. Rev. 1148, 1148 n.1 (1979).

staff assistant to Senator Edward Kennedy, chairman of a Senate subcommittee on health, insisted that the "only way" the objectives of Senator Kennedy's subcommittee could be achieved was to "publicize specific price and cost data for individual products."

GAO finally concluded that it had "no viable alternative than to press the companies for access to their cost data." Initially however, GAO sought the voluntary participation of drug manufacturers. Its appeal was successful; SmithKline and five other manufacturers voluntarily participated in the first phase of a proposed two-phase study. In April 1974, GAO issued a proposal for "Phase II," designed to "gather and develop the data necessary" to make a "presentation concerning salient economic and operational aspects of the industry." The study was to cover research and development, manufacturing, marketing, distribution, and corporate overhead. GAO requested data relevant to all these aspects of the companies' business for the period between 1964 and 1973.

SmithKline expressed reservations about giving GAO access to such cost and pricing data without adequate guarantees of confidentiality. The Comptroller was prepared to give such guarantees in the interests of completing the study. Between April and August of 1974, GAO representatives met with Senate staff to seek their consent to the assurances of confidentiality. GAO emphasized that it would obtain "far more data" from voluntary disclosure, obtained on the basis of guaranteed confidentiality, "than we could demand under our statutory authority." The staff members were unpersuaded and refused to sanction any assurances of confidentiality.

On August 26, 1974, abandoning the concept of a voluntary study, the Comptroller issued formal demand letters, seeking access to the records of the companies that had participated in the Phase I study. This step was taken with the approval of Senator Nelson. GAO was un-

der no legal obligation to accede to the Senators' demands, and the demands had not been formally made by their respective subcommittees. GAO's sole reason for abandoning its voluntary program and resorting to formal demands was the Senators' refusal to approve any assurances of confidentiality.

GAO had no reason to believe that any impropriety had occurred in connection with the contracts, that any excess or unfair profits had been made, or that any violation of the law or other irregularity had occurred. All of the contracts selected by GAO for demand letters were fixed-price procurements, with prices established not by actual negotiation, but by reference either to catalogue prices for ordinary commercial items sold in significant quantities to the general public or to other evidence of a competitive price.

SmithKline filed this action seeking a declaratory judgment that the Comptroller lacked the authority to require the production of the data demanded.[2] The Government counterclaimed for declaratory and injunctive relief to compel SmithKline to comply with the Comptroller's demand. The district court granted the Government's motion for summary judgment, holding that GAO shall have access to all of SmithKline's cost records that the Government contended were directly pertinent to the price of the drugs sold under the contracts.

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2. This case is one of several recent challenges to the Comptroller's authority to examine the records of pharmaceutical companies pursuant to the access-to-records provisions. *See United States v. Abbott Lab.*, 597 F.2d 672 (7th Cir. 1979); *Eli Lilly & Co. v. Staats*, 574 F.2d 904 (7th Cir.), *cert. denied*, 439 U.S. 959 (1978); *Merck & Co. v. Staats*, No. 74-1447 (D.D.C. August 12, 1977), *aff'd per curiam*, Nos. 79-1435, 79-1438 (D.C. Cir. September 10, 1981); *Bristol Lab. Div. of Bristol-Myers Co. v. Staats*, 428 F. Supp. 1388 (S.D.N.Y. 1977), *aff'd per curiam*, 620 F.2d 17 (2d Cir. 1980), *aff'd by evenly divided court*, 101 S. Ct. 2037 (1981).

II.

SmithKline makes two main arguments on appeal: (1) that GAO sought information from SmithKline for an improper purpose; and (2) that the scope of the demand exceeds that allowed by the access-to-records provisions. The improper purpose argument raises three distinct issues: (a) whether GAO exceeded its statutory authority to audit the performance of particular Government contracts by demanding access to confidential financial records for the purpose of conducting a general study of procurement techniques or of conducting an economic survey of the profitability of the pharmaceutical industry; (b) whether GAO exceeded its statutory authority by demanding access to confidential financial records, at the instance of two Senators and their staff aides, in order to furnish the Senators with individual company and product data through the conduct of an economic survey of the profitability of the pharmaceutical industry; and (c) whether the district court erred in granting summary judgment because the court's interpretation of the record created a material factual issue regarding the actual purpose of GAO's demand.

SmithKline's arguments are premised on the principle that an agency that is given power to investigate for one purpose cannot use that power to pursue distinctly different, unauthorized goals. *See, e.g., United States v. LaSalle National Bank*, 437 U.S. 298, 307, 316-17 n.18 (1978) (IRS subpoena power); *United States v. Garden States National Bank*, 607 F.2d 61, 68 (3d Cir. 1979) (same); *United States v. Humble Oil & Refining Co.*, 488 F.2d 953, 954 (5th Cir. 1974) (holding that the IRS exceeded its authority in issuing a summons in furtherance of a project for which the primary purpose was research rather than the investigation and adjustment of tax liabilities), *vacated and remanded*, 421 U.S. 943, *reaff'd*, 518 F.2d 747 (5th Cir. 1975); *Burlington Northern, Inc. v. ICC*, 462 F.2d 280, 286 (D.C. Cir.) (ICC re-

quest for an injunction), *cert. denied*, 409 U.S. 891 (1972). Assuming, without deciding, that the contractual powers of GAO, a unique independent agency within the legislative branch, are subject to the same restraints as those on the subpoena powers of administrative agencies,[3] we proceed to examine whether the undisputed facts support SmithKline's assertion that GAO sought access for an improper purpose.

A.

SmithKline argues that GAO exceeded its limited authority to audit the performance of particular contracts under 10 U.S.C. §2313(b) and 41 U.S.C. §254(c) because it demanded access to confidential records for the stated purpose of conducting a general study of procurement techniques. The critical premise of such a position is that Congress enacted the access-to-records provisions to prevent profiteering and fraud, and not to sanction a general scrutiny of procurement techniques or an economic survey of a particular industry. According to SmithKline, Congress sought to deter specific abuses and not to permit general investigations of the records of companies which are not in any way suspected of fraud or impropriety in their dealings with the Government.

The provisions were certainly intended to authorize access to records in cases of suspected fraud and profiteering. *See, e.g.*, 97 Cong. Rec. 13,200 (1951) (remarks of Rep. Riehlman); 96 Cong. Rec. 17,123 (1951) (remarks of Rep. Celler). Nevertheless, given that such was the primary concern, it does not necessarily follow that

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3. *See Eli Lilly & Co. v. Staats*, 574 F.2d 904, 909 (7th Cir.), *cert. denied*, 439 U.S. 959 (1976); Cibinic & Lasken, *The Comptroller General and Government Contracts*, 38 Geo. Wash. L. Rev. 349, 350 (1970) (GAO operates "on the hazy borderline between legislative and executive powers"). *Cf.* Case Comment, *supra*, at 1154-56 (discussing whether GAO is an agency).

no other purposes for the provisions exist. There is a fine line between profiteering and wastefulness, and the vast majority of the legislative references to the provisions do not indicate an intent to restrict their use to situations involving impropriety. The problems of noncompetitive pricing detailed in the congressional debates include waste in Government procurement. Representative Hardy, the sponsor of the access-to-records provisions, summarized the congressional purpose as follows: "The major purposes of this bill are twofold: One, to give the Comptroller General the proper tools to do the job the Congress has instructed him to do; and, two, to provide a deterrent to improprieties and wastefulness in the negotiation of contracts." *Id.* at 13,198. Representative Hardy further explained that examination of contractors' records by the Comptroller would enable "the General Accounting Office to look behind the [price] which had been established [to assess whether it was] excessive" and would act as a "safeguard against waste and extravagance" in Government procurement. *Id. Cf. Schwegmann Brothers v. Calvert Distillers Corp.*, 341 U.S. 384, 394-95 (1951) (sponsor's statement of purpose is persuasive indication of congressional intent). Representative Hoffman remarked in the course of the debates that "GAO is the most effective agency we have against fraud and extravagance and waste and all those things." 97 Cong. Rec. 13,373 (1951). *See id.* at 13,199 (remarks of Rep. Hardy) (Congress "clearly understood . . . that there are a lot of other situations besides those involving fraud which might be uncovered").

SmithKline points to passages in the legislative history indicating that Congress intended only to detect fraud and profiteering with the access provisions. *See id.* at 13,373 (remarks of Rep. Hardy) (reassuring the House that exercise of the provisions would not be routine but that GAO could invoke them if it has "reason to suspect fraud or bad faith or illegality" in connection

with the contract); *id.* at 12,611 (remarks of Rep. Hardy) (stating the "sole purpose of the bill is to enable the Comptroller General to make effective audits along the lines and under the jurisdiction conferred upon the General Accounting Office by law"). We are not convinced, however, that these scattered statements are indicative of the thrust of the legislative history. The most reasonable construction of the access-to-records provisions is that Congress has authorized GAO to uncover waste by invoking them.

We also find support for our interpretation of the statute and its legislative history in the case law. *See Merck & Co. v. Staats*, Nos. 79-1435, 79-1438, slip op at 3 (D.C. Cir. September 10, 1981) (Mikva, J., concurring in part and dissenting in part); *United States v. Abbott Laboratories*, 597 F.2d 672, 674 (7th Cir. 1979); Eli Lilly & Co. v. Staats, 574 F.2d at 915-16. *But cf.* Note, *Government Contracts: Contractor's Obligation to Allow Examination of Records Under 10 U.S.C. §2313(b)*, 72 Dickinson L. Rev. 687, 691 (1968) (stating that access provisions were intended "solely to provide a method to discover fraudulent activities," but recognizing that "there is nothing in the Act specifically negating" the possibility that Congress sought to improve general procurement techniques).

Although the statute and its legislative history do not specifically indicate that Congress intended to authorize GAO studies of procurement techniques, they authorize GAO to seek information that will help the Government reduce wastefulness and that is "directly pertinent" to the contract. Acquiring data for studies of procurement techniques seems a reasonable means to the end that Congress intended. In light of our own review of the statutes and their legislative history, we are unpersuaded that GAO's interpretation of the access-to-records provisions as allowing such access is unreasonable. *See Hewlett-Packard v. United States*, 385 F.2d

1013, 1016 (9th Cir. 1967) (noting that, if production costs are "out of line with the contract price, the contract may have been an inappropriate means of meeting this particular procurement need. . . . [and this approach] could lead to the use of other methods of meeting future procurement needs"), *cert. denied*, 390 U.S. 988 (1968).

Great weight is traditionally accorded to the construction of a statute by the agency charged with its administration "unless there are compelling indications that it is wrong." *Red Lion Broadcasting Co. v. FCC*, 395 U.S. 367, 381 (1969). SmithKline points to evidence that GAO has expressly and impliedly indicated, in letters to congressional committees at the time the statute was enacted, in internal memoranda, and in recommendations that Congress grant it additional authority, that it lacks the power to examine records relating to nongovernment business activities or to conduct "should cost" studies. SmithKline also contends that GAO has never previously conducted economic "industry" studies. At the most, SmithKline's evidence suggests that the GAO has changed its interpretation. More likely, GAO's interpretations represent GAO's search to discover which tasks are reasonably related to its responsibility for overseeing Government purchases. In any case, we believe that GAO has correctly concluded that it has the statutory authority to make the studies that it has proposed.

Nor do we think it determinative that Congress has only once granted GAO a right of access to records of government contractors for the purpose of conducting an economic study, or that in 1973 and 1975 Congress declined to act on several proposals drafted by GAO that would have granted GAO access to contractors' records in order to conduct profit studies of Government contractors. *See, e.g., American Trucking Associations v. Atchison, Topeka & Santa Fe Railway*, 387 U.S. 397, 418 (1967) (agency's request for legislation is not re-

garded as administrative interpretation of enabling statute); *United States v. UMW*, 330 U.S. 258, 281-82 (1947) (subsequent legislative history declaring intent of an earlier statute not controlling). Relying on the fact that Congress did not pass a bill to interpret a bill that Congress passed many years earlier is inherently suspect. Such inaction certainly does not indicate that Congress itself has concluded that the provisions themselves do not grant authority for the studies. The issue here is whether the access-to-records provisions now before us can reasonably be read to permit the GAO's present demand. We conclude that they can.

Assuming that GAO actually seeks SmithKline's records for the purpose of conducting an economic study of the pharmaceutical industry, we believe that it is a small step to find that the Comptroller's audit responsibilities include the study not only of the firms that contract with the Government but also the industries of which the firms are a part. GAO must have some understanding of an industry before it can study an individual procurement effectively. The Comptroller's Phase II demand in this case is equivalent to a request for access to records relevant to a cost-price comparison of each contract for the purpose of determining whether there has been "wastefulness" in pharmaceutical procurement. That the GAO will facilitate its comparison by compiling an industrywide economic study or procurement techniques study does not vitiate that purpose.

B.

SmithKline also argues that the record clearly demonstrates that GAO seeks access to SmithKline's confidential business records to undertake an economic study of the pharmaceutical industry in response to intense and continuing pressure from two Senators and their staff aides who wish to obtain, for public disclosure cost and pricing data relating to specific products and manu-

facturers.[4] Assuming, as we must, for purposes of reviewing the district court's summary judgment, that SmithKline could prove that GAO is seeking to obtain information for an industrywide economic study that would provide Senators Nelson and Kennedy with the information they sought, we cannot hold that GAO's purpose is improper. The statutory requirement that the access-to-records provision be included in the contracts establishes the public interest in uncovering wastefulness and extravagance. That United States senators encourage and influence GAO to use its powers to the fullest extent allowed by law, and that GAO heeds those Senators, is irrelevant. *See* Parnell, *Congressional Interference in Agency Enforcement: The IRS Experience*, 89 Yale L.J. 1360, 1368 (1980), quoting *Gravel v. United States*, 408 U.S. 606, 625 (1972) (noting that "members of Congress 'are constantly in touch with the Executive Branch of Government — they may cajole, and exhort with respect to the administration of a federal statute' "). We believe that a demand letter issued by GAO pursuant to its statutory authority, under the continuing and intense pressure of United States senators, may not, with-

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4. We do not understand SmithKline's argument to be that, assuming GAO lawfully has acquired information — under the pressure from the Senators — for the purpose of preparing an industrywide economic study, it cannot turn it over to individual senators. Rather, we believe that SmithKline's argument is simply that "the central purpose underlying the Comptroller General's demands was to obtain exploitable cost information, desired by two Senators and their aides, through the conduct of a broadranging study of the economics of the pharmaceutical industry." We therefore need not address what limits, if any, exist on GAO's ability to disclose information obtained by invocation of the access-to-records provisions.

The parties have agreed to provisions that substantially protect the confidentiality of the records. *See SmithKline*, 483 F. Supp. at 723-24 (confidential information may only be disclosed if: (1) identification of SmithKline as the source of the information is impossible; (2) if a committee or chamber of Congress requests the information; or (3) if a subpoena is issued for the information).

out more, be resisted on the ground that GAO sought the information for an improper purpose.

In *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d 118 (3d Cir. 1981) (en banc), we indicated that "we will not countenance judicial interference with agency decisions to conduct investigations, decisions that are committed entirely to agency discretion. . . ." *Id.* at 127 (citing, e.g., *City of Chicago v. United States*, 396 U.S. 162, 165 (1969)).[5] The reason for this policy of noninterference was recently stated by the United States Court of Appeals for the Fifth Circuit: "Judicial supervision of agency decisions to investigate might hopelessly entangle the courts in areas that would prove to be unmanageable and would certainly throw great amounts of sand into the gears of the administrative process." *Dresser Industries, Inc. v. United States*, 596 F.2d 1231, 1235 n.1 (5th Cir. 1979), *cert. denied*, 444 U.S. 1044 (1980). We believe those same concerns support our result in this case. Moreover, although the courts that have considered whether GAO may investigate fraud and whether it was motivated by a proper purpose in investigating the pharmaceutical industry have taken an approach different from our own, *see Lilly*, 574 F.2d at 910-12 (finding speculation about senatorial prodding unnecessary if GAO otherwise has a legitimate purpose); *Merck*, slip op. at 4-5 (Mikva, J., concurring in part and dissenting in part) (same); *SmithKline*, 483 F. Supp. at 720-21, no court has found that GAO is pre-

5. In *Wheeling-Pittsburgh*, this court recognized that the enforcement of an SEC subpoena may be challenged where the agency is abusing the court's process. *See* 648 F.2d at 125. Although this case was called to counsels' attention at oral argument, SmithKline does not contend that this case is controlling in the present circumstances. Indeed, SmithKline does not allege that GAO is acting in bad faith in seeking access to the information. *Cf. id.* at 125 n.9 (defining agency bad faith as "a conscious decision by an agency to pursue a groundless allegation without hope of proving that allegation").

cluded from demanding records from pharmaceutical firms because of an improper purpose.

C.

SmithKline argues that at a minimum this court must decide that material issues of fact regarding the actual purpose of the Comptroller exist, thus rendering summary judgment for the Government inappropriate. We have concluded, however, that, assuming GAO sought to conduct a broad economic study of the pharmaceutical industry in order to provide cost and pricing data to individual Senators, GAO did not invoke the access-to-records provisions for an improper purpose. Thus, SmithKline's contention is without merit, because the issue as to the Comptroller's actual purpose is not material to our legal conclusion.

III.

SmithKline also alleges that the district court erred in its determination of which records may be considered "directly pertinent" to "transactions relating to" the contracts. SmithKline makes two arguments as to the scope of access: (1) cost records are pertinent only to cost-based contracts; and (2) even if some cost data is pertinent to fixed-price contracts, the district court failed to set any reasonable limits on the scope of GAO's access.

A.

The five contracts at issue are fixed-price contracts. The prices were established by reference either to catalogue prices for ordinary commercial items sold in significant quantities to the general public or to other evidence of competitive price. SmithKline argues that cost data cannot be "directly pertinent" to "transactions related to this contract" where the price is fixed not in refer-

ence to a standard of fairness in negotiating or to costs, but to catalogue, market, or competitive prices. In support of this interpretation of sections 2313(b) and 254(c), SmithKline points to limitations in the Truth-in-Negotiations Act, 10 U.S.C. §2306(f) (1976), and in the Renegotiation Act of 1951, 50 U.S.C. §1216(e) (1976), on the submission of cost data for the negotiation or renegotiation of contracts based on established catalogue prices or adequate price competition. SmithKline argues that these statutes and the regulations promulgated thereunder provide important evidence that similar restrictions are incorporated in sections 2313(b) and 254(c) through the language limiting access to material "directly pertinent" to "transactions relating to" the contract. SmithKline contends that, in the absence of convincing evidence that different interpretations were intended, interrelated statutory provisions should be given a harmonious construction. *See Kokoszka v. Belford*, 417 U.S. 642, 650 (1974). SmithKline maintains that in this area of Government procurement Congress has consistently recognized that the presence of competition is a sufficient substitute for other safeguards against contractor abuse.

Both the statutory and the contractual provisions clearly apply by their terms to negotiated contracts without qualification. If Congress had desired to exclude fixed-price contracts from the provisions' operation, it could have explicitly done so, as it did in the Truth-in-Negotiations Act and in the Renegotiation Act. *See Lilly*, 574 F.2d at 916; *Hewlett-Packard*, 385 F.2d at 1016. Moreover, SmithKline's contention that the access-to-records provisions do not extend to costs conflicts with the language of the provisions. Not only has SmithKline contracted to disclose some "directly pertinent" records in its possession, but it has also contracted to put a provision in its subcontracts securing access for GAO to the "directly pertinent" records of its subcontractors. If the position now urged by SmithKline that the

statute and contract do not allow access to any cost records is correct, the provision for access to the records of SmithKline and of its subcontractors would be a nullity. The purpose of the access-to-records provision is to allow GAO to assess the reasonableness of the contractors' costs and pricing by insuring full access by the Comptroller to all directly pertinent cost and pricing records, including subcontractors' records that otherwise might be unreachable because they would not be in the custody and control of the contractor. Thus, SmithKline's reading ignores a large portion of the provision itself and violates the well-established rule that a contract and a statute should be read so as to give meaning to all their provisions.

SmithKline argues that, because the access-to-records provisions are dictated by statute, they cannot be individually tailored to meet the specific requirements of each contract. The Government, SmithKline contends, can take no comfort from the fact that the access clauses seem to envisage the production of subcontractor records that appear to be relevant to the issue of costs and pricing. This clause is required by the statute whether or not SmithKline planned to use subcontractors in the performance of the particular contract. SmithKline argues that similarly the clause is required whether the subcontractor's performance will be "directly pertinent" to the particular contract or not.

Congress has by statute required a provision in every contract that in some instances has no application because the contractor does not employ a subcontractor. The possibility that a standard contractual provision will have no application in one contract does not, however, render it meaningless in another contract where it could have application. Thus, we think that cost records can be directly pertinent to fixed-price contracts and that an access-to-records provision in such a contract gives GAO the authority to request directly pertinent data. *See Lilly*, 574 F.2d at 916.

B.

Determining that the statutory provision does not exempt fixed-price contracts does not necessarily mean that all costs that affect the price of the drug covered in the contract are directly pertinent to the contract. Representative Hardy used the following examples to illustrate the situations which his bill was designed to reach:

> It is common practice today to provide in a contract for construction work a fixed overhead rate, either as a proportion of direct labor costs or as a lump sum amount. . . .
>
> If in the course of checking the accounts of the accountable officer, the GAO found a situation indicating that the amount of overhead charged under the Government contract was a great deal higher than the amount paid under a private contract for the same work, it would then obviously be desirable for the General Accounting Office to look behind the rate which had been established. . . .
>
> During the last war, there were cases where contractors held both fixed-price and cost-plus-a-fixed-fee contracts covering similar items or services, both contracts being performed simultaneously and in the same plant. In several cases it was found that the contractor was charging to the cost-plus-a-fixed-fee contract expenses which should have been charged to the fixed-price contract. In that way he was being reimbursed for expenses which should have been paid out of his own pocket. Such a practice may, or may not, have been intentional. But in any event, there would be little or no chance of detecting such a practice, unless the General Accounting Office has access to the contractors' books and records.

97 Cong. Rec. 13,198 (1951). For GAO to detect a differential allocation of overhead costs between governmen-

tal and nongovernmental contracts, or between cost-plus and fixed-price contracts, it would have to examine a very broad set of records. *See* Case Comment, *supra*, at 1157-58 n.67. The implication of Representative Hardy's examples is that the legislation was intended to authorize inquiry not only into all costs associated with each negotiated government procurement contract, but also into all similar contracts between a particular contractor and his private buyers, in order to determine whether the government was bearing an excessive share of the company's fixed costs. It is clear, however, that Congress did not intend the "directly pertinent" language to allow GAO to examine records of costs recovered exclusively from nongovernmental contracts. *See Merck*, slip op. at 27 (Mikva, J., concurring in part and dissenting in part); Memorandum on the Adequacy of the Legal Authority of the General Accounting Office to Conduct a Comprehensive Study of Profitability in Defense Contracting, *reprinted at* 115 Cong. Rec. 25,800 (1969) [hereinafter GAO Memorandum] (GAO has taken the position "that the words 'directly pertinent' were intended only to limit GAO's right of access to records pertaining to Government work as distinguished from non-government work").

The bill that contained sections 2313(b) and 254(c) originally limited the Comptroller to "pertinent" records of the contractor. Representative Hoffman emphasized in debates over the access-to-records provision that he objected strongly to "snooping expeditions" and that the access-to-records provisions would allow GAO "unlimited authority to go everywhere and snoop into everybody's business." 97 Cong. Rec. 13,373 (1951) (also stating opposition to a statute that "would let GAO go into everybody's business and look it over"). To prevent an expansive interpretation of the provisions, Congress restricted the access proposal even further, by specifying that only records "directly" pertinent to the contract may be demanded. Representative Hoffman,

who sponsored the limiting amendment but opposed the original bill, *see* 97 Cong. Rec. 13,377 (1951), stated specifically that the purpose of the modifying language was to "limit the 'snooping' that may be carried on under this bill." *Id.* Representative Hoffman emphasized that, unless the proposed bill were limited, even a small government contract would open all of a contractor's records to inspection by GAO. He pointed out that, without amendment, the provisions would permit a contract for ten percent of a contractor's production to be inspected by GAO "not only with reference to that one item of 10 percent . . . but into all of his other business where that same item was used." *Id.* He feared this result because the contractor would inevitably fail to keep "a separate set of books" for his government business, so that: "every section of his books will have to come under the complete scrutiny of the GAO. He is going to be harassed no end to try to break down production costs and show the details. . . ." *Id.* at 13,376 (remarks of Rep. Harvey). Although these statements were offered in support of a proposed amendment relating to subcontractors, we believe that the same apprehension stimulated the introduction and adoption of the limiting "directly pertinent" language.

The Government argues that Congress' addition of the word "directly" did not sharply narrow the scope of inquiry to be allowed GAO. *See* Case Comment, *supra*, at 1157-58. *But see* Note, Eli Lilly & Co. v. Staats: *An Undue Expansion of the GAO's Investigatory Power Under the Access-to-Records Statutes*, 74 Nw. U.L. Rev. 122, 135 (1979) [hereinafter Nw. Note]. It is true that Representative Hardy did not oppose the amendment. *See* 97 Cong. Rec. 13,377 (1951). It is also true that Representative Hoffman did not indicate how his change would affect GAO's ability to secure specific documents. *See id.* On the other hand, a sponsor's statement of purpose generally is regarded as a persuasive indicator of congressional intent. *See Federal Energy Administra-*

tion v. Algonquin SNG, Inc., 426 U.S. 548, 564 (1976). In any case, we do not believe that the insertion meant nothing just because there was little debate on the change.

The legislative history manifests a strong congressional intent to prevent unlimited "snooping." "[W]hen Congress enacts a statute designed to limit government intrusion in the private affairs of its citizens, the statutory provisions must be followed scrupulously." *United States v. Bacheler*, 611 F.2d 443, 447 (3d Cir. 1979). We thus conclude that the contract does not provide for unlimited access to SmithKline's cost records.

When cost information is not allocated to specific contracts and their products, the Government's argument that generalized cost data are "directly pertinent" to any given contract is weakened. *See* Nw. Note, *supra*, at 132. Like most manufacturing businesses, SmithKline divides its costs into a small category of direct manufacturing costs that can be readily assigned to a particular product and into other categories of cost, including research and development, distribution, marketing, advertising, and administrative costs, which are not assigned to any one product. *See* Reekie, *Price and Quality Competition in the United States Drug Industry*, 26 J. Indus. Econ. 223, 235 (1978); Nw. Note, *supra*, at 132-33. *Cf.* National Association of Cost Accountants, *Research Series No. 29, Accounting for Research and Development Costs*, 36 N.A.C.A. Bull. 1375, 1427-30 (1955) (survey finding that some businesses assign research and development costs to particular products, but some do not because the arbitrary method of allocation would not be helpful). SmithKline maintains that this common practice reflects the lack of generally accepted accounting principles that permit accurate and meaningful allocation of these indirect costs.

Obviously, however, these unassigned costs affect the price charged for the company's products, because the company must recover both the costs directly as-

signed and the unassigned pooled costs. Manufacturing and distribution costs of individual pharmaceutical products may constitute as little as nine percent of the products' sale price. *See Lilly*, 574 F.2d at 913; Rucker, *Public Policy Considerations in the Pricing of Prescription Drugs in the United States*, 4 Int'l J. Health Services 171, 173 (1974).By characterizing unallocated costs as "directly pertinent" to government procurement contracts, GAO would be able to demand access to all records of pooled costs whenever the price charged the Government in the contracts at issue reflects costs attributable to the pool. GAO would thus have access to most, if not all, of SmithKline's pricing data.[6]

The Government, on the other hand, rejects both the argument that there are no generally accepted accounting principles that permit meaningful allocation of these indirect costs and SmithKline's suggestion that GAO's interpretation of the access provision would be without limits. The Government argues that SmithKline itself allocates costs to products and performs profitability studies for its own purposes; even if allocation of indirect costs to products cannot be made with scientific accuracy, it is helpful and necessary. The Government contends that there is almost no limit to the allocation of costs to particular products other than that set by expediency. The Government maintains, however, that it will not need certain information or information breakdowns and thus that its request for information is not without bounds. In short, the Government's contention is that any cost affecting the prices charged the Government under a given contract may be "directly pertinent" to the

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6. If GAO were allowed access to this information, it would presumably have to make a similarly arbitrary allocation. Thus, denying or granting access to such records will have little effect on GAO's ability to evaluate the contractor's pricing practices on a *particular* contract. *See* Nw. Note, *supra*, at 134. The information would, however, be useful in determining the extent of differential allocation between contracts.

contract. *See Lilly* 574 F.2d at 914-15 (finding that an item is directly pertinent to a contract if it is a "significant input" in the price of the product purchased in the contract).

We believe that the Government's argument undermines its own position, for it would seem that the Government's interpretation of "directly pertinent" admits of no doctrinal limitation on its access powers. We are unwilling to read the statutory provision as granting to GAO such broad discretion in determining what is pertinent and what is "snooping." The Government has not suggested a definition of "directly pertinent" that preserves the distinction between snooping and properly limited access. Indeed, its argument gives the phrase no effect in this case. If a "directly pertinent" cost record means any cost having a significant input into price, it would seem that GAO could also justify an extensive investigation of subcontractors who may actually be doing no Government business at all. *Cf.* Morgan, *The General Accounting Office: One Hope for Congress to Regain Parity of Power with the President*, 51 N.C. L. Rev. 1279, 1364-65 (1973) ("The same argument that would justify a GAO audit in *Hewlett-Packard* would justify an audit of contractors doing no government business at all."). We do not think that an interpretation of the "directly pertinent" language that allows practically unlimited investigation of companies that do no direct business with the Government can be sound in light of the congressional desire to prevent snooping.

The Government contends that GAO's administrative interpretation of "directly pertinent" should be followed in the absence of "compelling indications that it is wrong," especially where those interpretations were reported to Congress. We believe, however, that Congress' inaction in the face of the report should not be read as acquiescence. *See Girouard v. United States*, 328 U.S. 61, 69 (1946). GAO's broad interpretation of the provisions is inconsistent with the congressional intent and is

entitled to no deference. *Cf.* Nw. Note, *supra*, at 135 n.77 ("The GAO itself has been uncertain about the exact limits of its authority under the access-to-records statutes."). We must therefore search for a more limited interpretation if "directly pertinent" is to be given an interpretation consistent with the congressional history.

In some industries, costs such as research and development have such a small impact that they arguably are not "directly pertinent" to the contract and its price. *See Lilly*, 574 F.2d at 913-14. Whether a cost record is "directly pertinent" could vary from industry to industry. *See Merck*, slip op. at 26-27 (Mikva, J., concurring in part and dissenting in part). In some industries, direct costs are the predominant component of a product's price, and there would be no need to grant access to indirect cost information of those firms. But in the pharmaceutical industry, research and other costs not immediately attributable to one product form a large part of the costs of a pharmaceutical product. Each case could be decided on its facts by addressing one question: whether the records sought will show production costs and pricing of the contracts sufficient to determine why the contract price was fixed as it was and whether "the contract may have been an inappropriate means of meeting this particular procurement need of the Government." *Hewlett-Packard*, 385 F.2d at 1016. The judicial decision as to what records are necessary would thus be essentially an accounting problem which is not unlike those problems which are common in day-to-day discovery involving corporations. *See generally United States v. IBM Corp.*, 66 F.R.D. 186 (S.D.N.Y. 1974); Fed. R. Civ. P. 33(c).

Although it is tempting to take the opportunity to make the decision as equitably as possible in each case, we are not convinced that Congress intended for the interpretation of the access-to-records provision to depend on the facts of each case. The same provision appears in

most Government contracts. *See* Nash, *Risk Allocation in Government Contracts*, 34 Geo. Wash. L. Rev. 693, 694 n.3 (1966) (finding that only one quarter of all Government procurement contracts are advertised procurements). We believe that Congress intended the words to acquire some common meaning so that the Government and the contracting firm could know within reason what they were contracting to perform. In contracts involving many millions of dollars, many firms, and many products, certainty is more important than deciding each case on its facts.

In *Bristol Laboratories Division of Bristol-Myers Co. v. Staats*, 428 F. Supp. 1388 (S.D.N.Y. 1977), *aff'd per curiam*, 620 F.2d 17 (2d Cir. 1980), *aff'd by evenly divided court*, 101 S.Ct. 2037 (1981), the district court equated the directly pertinent costs with "manufacturing costs (including raw and packaging materials, labor and fringe benefits, quality control and supervision); manufacturing overhead (including plant administration, production planning, warehousing, utilities, and security); royalty expenses; and delivery costs." 428 F. Supp. at 1389. *See id.* at 1391. Specifically excluded, however, were data with respect to "research and development, marketing and promotion, distribution and administration (except to the extent that these areas may be included in the factors above)." *Id.* at 1389-90. The Government has not put forward an alternative definition of "directly pertinent" records that we should adopt if we do not agree with its interpretation of the statute. We therefore adopt the standard formulated in *Bristol*, which for the most part relies on the distinction between direct and indirect costs. We believe that it comports with Congress' intent to preclude GAO's scrutiny of nongovernmental contracts. Moreover, our distinction between information that is "directly pertinent" and that which is not follows the distinction drawn by every circuit to consider the issue with the exception of the Sev-

enth Circuit.[7] *See Merck*, No. 74-1447, slip op. 4-5 (D.D.C. August 12, 1977), *aff'd per curiam*, Nos. 79-1435, 79-1438 (D.C. Cir. September 10, 1981).

The Government argues that GAO's interpretation that the access-to-records provision provides for the access it seeks here has been well-known and judicially established since the *Hewlett-Packard* decision in 1967. We do not believe, however, that the Ninth Circuit sanctioned access to all indirect overhead cost data. The Ninth Circuit held that GAO should have access to "production costs." 385 F.2d at 1016. Although the court never defined these costs, the district court's order, affirmed by the court of appeals, referred specifically to "costs of direct material, direct labor and overhead costs." *Id.* Our decision includes direct costs and some overhead within its definition of "directly pertinent." How much overhead the Ninth Circuit intended to include is uncertain. *See Merck*, slip op. at 23 n.27 (Mikva, J., concurring in part and dissenting in part) ("Later decisions have disagreed over the *Hewlett-Packard* holding on this point."). *Compare Lilly*, 574 F.2d at 913, *with Bristol*, 428 F. Supp. at 1391. Thus, *Hewlett-Packard* does not necessarily suggest a result contrary to that in our case.

We have concluded that GAO may demand access to detect wastefulness and may make certain studies to help it in its task. We are aware, however, that the limiting interpretation that we have given the access-to-records provision may make it more difficult in some cases for GAO to obtain the information it may

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7. We note that in *Abbott Laboratories* another panel of the Seventh Circuit addressed precisely the same issues as those addressed in *Lilly*. The district court had granted summary judgment to the Government on the basis of *Lilly*, and the circuit court affirmed. Two of the three judges, however, specifically expressed reluctance and concurred in the affirmance solely because they considered themselves bound by the earlier decision. *See* 597 F.2d at 674 (Pell, J., concurring); *id.* at 675 (Wood, J., concurring).

need to uncover wastefulness.[8] Economic studies based on such restricted data may be of limited utility, and if the access provisions were meant to equalize the relationship between the Government and private contractors, our reading of the clause fails to advance fully that purpose in this case. *See* Merck, slip op. at 20-21 (Mikva, J., concurring in part and dissenting in part). The difficulty, however, arises because (1) the statute attempts to further the two conflicting congressional goals of limiting "snooping" and permitting broad access; and (2) the pharmaceutical industry presents special characteristics. The conflict in goals appears on the face of the statute itself. *Cf.* Nw. Note, *supra*, at 139 ("there can be no accommodation of the competing interests; either the GAO gets all of the information or it gets none of it"). For example, the fact that the demand is limited by the access-to-records provisions to data within three years of final payment, *see* 10 U.S.C. §2313(b), no doubt hampers the detection of wastefulness and the usefulness of any studies that are prepared. Congress also restricted GAO's investigatory powers by not making the access-to-records provisions applicable to advertised as well as negotiated contracts. Information on producers doing no business with the Government would undoubtedly also be useful in the overall improvement of Government procurements, since the data could be compared

8. In industries where direct costs are the prime component of price, where firms are producers of only one product, or where the firms sell almost everything they make to the Government, our decision will have little limiting effect on GAO's ability to make various studies. With other firms, manufacturing cost information alone might be useful for two purposes: (1) it might help to uncover fraud; and (2) where the products are part of a competitive market, which most fixed-price cost contracts, by definition, are, comparison of direct cost information could help the Government determine which company is assigning more overhead to its product. Nevertheless, we realize that our decision will limit to varying degrees GAO's ability to study any industry with firms that make several products or have several buyers.

with the data collected from companies contracting with the Government: but GAO cannot obtain that information under the provisions. *See* Morgan, *supra*, at 1364-65. We do not believe that we are free to ignore these limitations in trying to assure that GAO has meaningful access to the contractors' records.

GAO has itself recognized its dilemma: "While GAO's legal authority would permit it to perform some of the work necessary in making a profit study. . . ., to do a meaningful study of profitability . . . , legislation should be enacted broadening its right of access to records. . . ." GAO Memorandum, *supra*, *reprinted at* 115 Cong. Rec. 25,801 (1969). "In establishing the 'directly pertinent' standard as a limitation on the GAO's access rights, Congress apparently was willing to forego obtaining all the information that might be related to a government contract if the only alternative was to require a contractor to make available virtually all of its records." Nw. Note, *supra*, at 134-35 (footnote omitted). If "directly pertinent" information is not sufficient to make the Comptroller's investigation of certain industries complete, or if certain industries should be treated differently because of unique circumstances, Congress, and not this court, is better able to decide which information GAO needs to fulfill Congress' expectations.

SmithKline must allow GAO personnel to inspect its records with respect to manufacturing costs, manufacturing overhead, royalty expenses, and delivery costs. SmithKline need not produce data with respect to research and development, marketing and promotion, distribution and administration, except to the extent that these costs may be included in the manufacturing costs.

IV.

The order of the district court will be vacated and the case remanded for entry of an order consistent with this opinion.

A True Copy:

Teste: /s/ Sally Mrvos

Clerk of the United States Court of Appeals
for the Third Circuit

APPENDIX B

United States Court of Appeals

FOR THE THIRD CIRCUIT

No. 80–1464

SMITHKLINE CORPORATION, APPELLANT

VS.

STAATS, ELMER; COMPTROLLER GENERAL OF THE UNITED STATES, DEFENDANT,

UNITED STATES, INTERVENING PARTY DEFENDANT.

(D. C. Civil No. 75–0499)

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF PENNSYLVANIA

Present: SEITZ, *Chief Judge;* VAN DUSEN and HIGGINBOTHAM, *Circuit Judges.*

JUDGMENT

This cause came on to be heard on the record from the United States District Court for the Eastern District of Pennsylvania and was argued by counsel on July 16, 1981.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court, entered January 25, 1980, be, and the same is hereby vacated and the cause remanded for the entry of an order consistent with the opinion of this Court.

ATTEST:
/s/ Sally Mrvos
Clerk

December 28, 1981

APPENDIX C

UNITED STATES DISTRICT COURT, E.D. PENNSYLVANIA

Civ. A. No. 75-499

SMITHKLINE CORPORATION, *Plaintiff*,

v.

Elmer B. STAATS, Comptroller General of the United States, *Defendant*,

and

THE UNITED STATES OF AMERICA, *Intervenor-Defendant*.

January 24, 1980

Memorandum

RAYMOND J. BRODERICK, District Judge.

This action arises from a demand asserted by the General Accounting Office ("GAO") for access to books and records maintained by the plaintiff SmithKline Corporation ("SmithKline"). Plaintiff filed a complaint seeking declaratory and injunctive relief to bar GAO from access to the documents. The Court granted the motion of the United States to intervene as a party defendant for the purpose of asserting a counterclaim seeking declaratory and injunctive relief to compel SmithKline to comply with

GAO's demand for documents. Now before the Court are plaintiff's motion for summary judgment and the government's motion for summary judgment on its counterclaim. For the reasons hereinafter set forth, the Court will grant the government's motion for summary judgment on its counterclaim and deny the plaintiff's motion for summary judgment.

In determining the propriety of granting a motion for summary judgment, the Court must consider whether there exists a genuine issue as to any material fact. *Hicks v. ABT Associates, Inc.*, 572 F.2d 960, 967 (3d Cir. 1978); *Abdallah v. Caribbean Security Agency*, 557 F.2d 61, 63 (3d Cir. 1977); *Scott v. Plante*, 532 F.2d 939, 945 (3d Cir. 1976). On the basis of uncontroverted depositions and affidavits filed by the parties in connection with the motions for summary judgment, the Court finds that there is no genuine issue of material fact. The uncontroverted record may be summarized as follows:

The Veterans Administration ("VA") and Defense Supply Agency ("DSA") awarded certain negotiated fixed-price contracts for pharmaceutical products to SmithKline, and, in one instance, to SK&F Co., its wholly owned subsidiary. Those contracts are summarized as follows:

Veterans Administration

Contract Number	Date of Award	Contract Price	Final Payment Made
V797P-5835b	7/31/73	Est. $1,599,042.50	—
V797P-5892b	10/2/73	$ 137,148.00	—
Defense Supply Agency			
DSA120-74-C-0519	8/1/73	$ 105,431.74	12/26/73
DSA120-73-D-2968	4/16/73	$1,436,510.30	8/22/74
DSA120-74-C-2518	3/6/74	$ 12,058.20	8/13/74

Pursuant to 41 U.S.C. § 254(c),[1] the contracts with the VA incorporated the following clause:

Examination Of Records By Comptroller General

(a) This clause is applicable if the amount of this contract exceeds $2,500 and was entered into by means of negotiations, including small business restricted advertising, but is not applicable if this contract was entered into by means of formal advertising.

(b) The Contractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under this contract or such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Procurement Regulations Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers, and records, of the contractor involving transactions related to this contract.

(c) The Contractor further agrees to include in all his subcontracts hereunder a provision to the effect that the subcontractor agrees that the Comptroller General of the United States or any of his duly authorized representatives shall, until the expiration of 3 years after final payment under the subcontract or

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[1] 41 U.S.C. § 254(c) provides:

(c) All contracts negotiated without advertising pursuant to authority contained in this Act shall include a clause to the effect that the Comptroller General of the United States or any of his duly authorized representatives shall until the expiration of three years after final payment have access to and the right to examine any directly pertinent books, documents, papers, and records of the contractor or any of his subcontractors engaged in the performance of and involving transactions related to such contracts or subcontracts. . . .

such lesser time specified in either Appendix M of the Armed Services Procurement Regulation or the Federal Procurement Regulation Part 1-20, as appropriate, have access to and the right to examine any directly pertinent books, documents, papers and records of such subcontractor, involving transactions related to the subcontract. The term "subcontract" as used in this clause excludes (1) purchase orders not exceeding $2,500 and (2) subcontracts or purchase orders for public utility services at rates established for uniform applicability to the general public.

(d) The periods of access and examination described in (b) and (c), above, for records which relate to (1) appeals under the "Disputes' clause of this contract, (2) litigation or the settlement of claims arising out of the performance of this contract, (3) costs and expenses of this contract. as to which exception has been taken by the Comptroller General or any of his duly authorized representatives, shall continue until such appeals, litigation, claims or exceptions have been disposed of.

The same clause was included in the Defense Supply Agency contracts pursuant to 10 U.S.C. § 2313(b), which provides:

(b) Except as provided in subsection (c), each contract negotiated under this chapter shall provide that the Comptroller General and his representatives are entitled, until the expiration of three years after final payment, to examine any books, documents, papers, or records of the contractor, or any of his subcontractors, that directly pertain to, and involve transactions relating to, the contract or subcontract.

On January 19, 1971, Comptroller General Elmer B. Staats and other GAO representatives appeared before

the Subcommittee on Monopoly of the Senate Select Committee on Small Business at hearings concerning the status of competition in the pharmaceutical industry. Mr. Paul Shnitzer of the GAO General Counsel's Office testified that

> . . . there is a statute which was enacted in 1951 which says in effect that any negotiated contract awarded pursuant to either the Federal Property Act or the Armed Services Procurement Act, which would cover the two major acts, has to contain a provision which gives the General Accounting Office access to the books, documents, papers and records of the contractor or his subcontractors which relate to the contract.[2]

Mr. Gregory Ahart, Deputy Director of GAO's Civil Division, testified that

> . . . we are continuing our work in examining drug procurement systems and as part of that work we will be giving consideration to utilizing the authority which we have under the provision of the 1951 act which Mr. Shnitzer mentioned, and actually examine the costs of certain of the drug manufacturers.
>
> We have not decided how far we are going to go on this and the final plans are indefinite, but this will be given consideration as part of this continuing work and I am sure some of it will be done.[3]

Senator Gaylord Nelson then stated:

> I realize it may be a very complicated matter, but it would seem to me that all companies ought to be served notice and the GAO is going to utilize this

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[2] Subcommittee on Monopoly of the Senate Select Committee on Small Business, Hearings on Competitive Problems in the Drug Industry, January 19, 1971, at 8018.

[3] *Id.* at 8020.

statute. I think that we ought to take a look at some of those costs.[4]

After the hearings, Senator Nelson and his staff pursued their efforts to have GAO obtain documents from the pharmaceutical companies. On August 9, 1971, the Comptroller General asked Senator Nelson and his staff assistant, Ben Gordon, if their objectives would be served by composite, industry-wide cost data that would be representative of several companies and products, but not identifiable as to any particular company or product. Gordon responded that they preferred individual product and company data, which "should be made public."[5] Gordon continued to press GAO to obtain documentation of costs from the pharmaceutical companies. (Ahart Dep., Exhibits PA-14 through PA-22). Gordon demanded on behalf of Senator Nelson that GAO seek data "through the courts, if necessary." (*Id.*, Exhibits PA-16, PA-17). Gordon told GAO that Senator Nelson believed that GAO should seek data "without any strings attached" so that the information "could be used as needed." (*Id.*, Exhibit PA-19). A staff assistant to Senator Edward Kennedy told GAO that individual company and product data were essential, since the "only way" that Senator Kennedy's objectives could be achieved was to "publicize specific price and cost data for individual products." (*Id.*, Exhibit PA-27).

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[4] *Id.*

[5] Deposition of Gregory J. Ahart, Director GAO Human Resources Division, October 19, 1976 (hereinafter "Ahart Dep."), Exhibit PA-15. Mr. Ahart's deposition was taken in the case of *Merck & Co. v. Staats*, No. 74-1447 (D.D.C.), but the parties stipulated that the deposition transcript may be used in this action as if the deposition had been taken in this case. Exhibits to the deposition are referred to as "Exhibit PA", with an identifying number. Copies of the exhibits and deposition transcript have been filed of record.

As a result of these communications, GAO eventually concluded that ". . . there is no viable alternative than to press the companies for access to their cost data." (*Id.*, Exhibit PA -18).

Subsequent to a second appearance by the Comptroller General before Senator Nelson's Subcommittee on May 10, 1972, GAO began to implement a two-phase study of the economics and operations of the pharmaceutical industry. As a first step, GAO representatives met with representatives of the Pharmaceutical Manufacturers Association and its member firms.* The first phase of the study consisted of two or three day visits to the facilities of six drug manufacturers, including SmithKline. Phase I of the study, in which the drug manufacturers voluntarily agreed to participate, was "designed to obtain for GAO an understanding of the drug manufacturing industry and to enable GAO to develop a meaningful approach for the second phase of the study." (Ahart Aff. I ¶ 6).

Following the Phase I visits, GAO prepared a proposed plan for a detailed study (Phase II). The objective of this study was "to gather and develop data necessary for GAO to present a comprehensive and objective presentation to the Congress and the involved Federal agencies concerning the salient economic and operational aspects of the drug industry." (Ahart Aff. I ¶ 8). It was proposed that GAO request that major drug manufacturers provide data for the years 1964 through 1973 relating to sales, manufacturing cost, research and development expenditures, general and administrative expenses, marketing costs, distribution costs, capital investment, and all other costs associated with the pharmaceutical business. (Ahart Dep., Exhibit PA-10). Senators Kennedy and Nelson continued to insist that the study provide cost data specific to individual

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* Affidavit of Gregory J. Ahart, July 8, 1975 (hereinafter "Ahart Aff. I") ¶ 5.

products and companies. (Ahart Dep. Exhibits PA-27, PA-29).

Beginning in March, 1974, GAO held discussions with the six pharmaceutical firms concerning their willingness to participate in the Phase II plan. By June, 1974, it became clear that the firms would not voluntarily permit access to the data sought by GAO. (Ahart Aff. I ¶ 9). GAO therefore dropped its plans for the voluntary Phase II study and decided upon "a more modest study" which would be based on data obtained through access-to-record provisions in negotiated government contracts with drug companies. (*Id.* ¶ 10). GAO has described the purpose of this study as follows:

> GAO intends to use data obtained through the access-to-records clause contained in the specified contracts in a proposed review to determine the basis for the prices charged by the suppliers of the products procured by the Government under the specified contracts. In undertaking this review GAO intends to: (1) identity and verify the direct costs involved in the manufacture and distribution of these particular products (2) identify the makeup and amounts of indirect costs involved in the development, manufacture, distribution, and marketing of these products and (3) review other pertinent considerations taken into account by the suppliers in pricing these products.

(Ahart Aff. I ¶ 11).

On August 26, 1974, the Comptroller General wrote to the President of SmithKline:

> As you know, because of the increasing Federal involvement in the procurement of pharmaceuticals, the General Accounting Office has underway a review of the procurement of drugs by agencies of the Federal Government, including the pricing of drugs and

pharmaceuticals procured under negotiated contracts. This examination is being conducted at several drug companies, including SmithKline Corporation, and is being made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. § 53), the Accounting and Auditing Act of 1950 (31 U.S.C. § 67), and the authority of the Comptroller General to examine contractors' records under the contract provisions pursuant to 10 U.S.C. § 2313(b) and 41 U.S.C. § 254(c).

. . . . .

The purpose of this letter is to formally request that cost records pertinent to contracts listed on enclosure 1 be made available for our examination as provided by the terms of the negotiated contracts awarded to your company by the Defense Supply Agency and the Veterans Administration. We must request that you have the responsible officials at SmithKline Corporation make available to the General Accounting Office as required, all books, documents, papers, and other records directly pertinent to the contracts, *which include, but are not limited* to (1) records of experienced costs including costs of direct materials, direct labor, overhead, and other pertinent corporate costs, (2) support for prices charged to the Government, and (3) such other information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests. For your information, statements from the legislative history pertaining to the "Examination of Records" clause included in the contracts and our position on the duties and responsibilities that the clause imposes upon my Office are presented in enclosure 2.

SmithKline refused to comply with this formal request for records, and filed its complaint seeking declaratory and injunctive relief on February 20, 1975.

SmithKline does not question the government's authority, pursuant to 41 U.S.C. § 254(c) and 10 U.S.C. § 2313(b), to include in its negotiated contracts provisions concerning "access-to-records." Furthermore, SmithKline concedes that it voluntarily executed the contracts at issue in this case with full knowledge of the access-to-records provisions contained in each contract. SmithKline argues, however, that it should not be required to disclose the information demanded by the GAO in this case because the record before the Court supports the conclusion that GAO is seeking the information for an improper purpose. This improper purpose, SmithKline contends, is that the GAO is seeking information concerning profits in the pharmaceutical industry for dissemination to Congress and the public. If the Court does not accept this contention and grants summary judgment for plaintiff, SmithKline then argues that summary judgment must be denied because the question of GAO's purpose constitutes a genuine issue of material fact. Finally, SmithKline argues that, even if this Court should conclude that GAO's purpose is proper, the information demanded in this case is beyond the scope of the access-to-records provisions of the contracts and the statutes. The government, on the other hand, argues that the provisions in the contracts and the statutes entitle the GAO to examine all records directly related to the costs of production of the drugs which the government has contracted to purchase. The government further argues that the uncontroverted factual record before the Court establishes that the purpose underlying its demand for records is proper.

Identical demands by GAO for the cost records of other drug companies have resulted in litigation in other circuits. In *Bristol Laboratories v. Staats*, 428 F.Supp. 1388 (S.D.N.Y.1977), the Court entered an order granting summary judgment for the plaintiff and requiring the production of only those documents the plaintiff agreed to provide,

i. e., those related to direct manufacturing costs but not costs incurred in research and development, marketing and promotion, or distribution and administration. The Court in *Merck & Co. v. Staats*, No. 74-1447 (D.D.C.1977), adopted the order entered by the *Bristol* court. The Seventh Circuit has interpreted the access-to-records clauses to require broad access to cost records, including costs of research and development, whether or not pharmaceutical companies allocate such costs directly to the contracts. *Eli Lilly & Co. v. Staats*, 574 F.2d 904 (7th Cir.), *cert. denied*, 439 U.S. 959, 99 S.Ct. 362, 58 L.Ed.2d 351 (1978); *United States v. Abbott Labs*, 597 F.2d 672 (7th Cir. 1979). Hoffman-LaRoche, another drug company from which the GAO sought similar information, settled without litigation. *The Comptroller General's Authority to Examine the Private Business Records of Government Contractors*, 92 *Harv.L. Rev.* 1148, 1150 (1979). The delay in ruling on these cross-motions for summary judgment has been due, to considerable extent, to the agreement of the parties to await the outcome of litigation in other circuits.

We will deal first with SmithKline's contention that the question of the purpose for GAO's demand for records is a genuine issue of material fact. The standard for granting a motion for summary judgment is well established. *See Hicks v. Abt Assoc., Inc., supra* 572 F.2d at 967. We are mindful of our responsibility to resolve in favor of the non-moving party any doubt concerning whether there is a genuine issue of material fact. This court's examination of the depositions and affidavits submitted by the parties clearly shows that the government has met its burden of demonstrating that there are no genuine issues of material fact.

The government has submitted the deposition and affidavits, accompanied by voluminous exhibits, of Gregory J. Ahart, a senior GAO official. The only factual material that SmithKline has placed before the Court is the affidavit

of Kenneth A. Bower, its Vice President for Administration and Finance. Mr. Bower's affidavit raises the issue of confidentiality, which has been resolved by the protective order agreed upon by the parties. The Bower affidavit also sets forth SmithKline's interpretation of the term "directly pertinent" as it is used in the access-to-records statutes. Mr. Bower's affidavit does not address the issue of the government's purpose for seeking SmithKline's records. Thus, the Ahart deposition and affidavits are uncontroverted in this regard. A party opposing summary judgment on the ground that there exists a genuine issue of material fact must respond to an affidavit with more than a general denial. *Lockhart v. Hoenstine*, 411 F.2d 455, 459 (3d Cir. 1969). The Court should not assume the existence of a factual issue where none exists. *Id.* In this case SmithKline attempts to characterize a legal issue as a factual one precluding summary judgment for the government. The question before the Court, however, is not "What was GAO's purpose in seeking information from SmithKline?". The uncontroverted factual record before the Court establishes that GAO's purpose is to compare cost to price of drugs purchased under specified contracts to determine the adequacy of the protections afforded the government in the contract negotiation process (Ahart Aff. I ¶ 11, discussed in detail, *infra*). Whether or not this purpose is authorized by the access-to-records statutes is a question of law upon which summary judgment is clearly appropriate. *Evans v. S. S. Kresge Co.*, 394 F.Supp. 817 (W.D. Pa.1975), *aff'd*, 544 F.2d 1184 (3d Cir. 1976), *cert. denied*, 433 U.S. 908, 97 S.Ct. 2973, 53 L.Ed.2d 1092 (1977).

SmithKline has agreed that "The relevant facts and issues here are identical to those in *Lilly* . . ." (Memorandum in Support of SmithKline's Cross-Motion for Summary Judgment), and has agreed to use discovery from previous cases. (*See* n. 5, *supra*.) Therefore, the denial of summary judgment in this already protracted and somewhat duplicative litigation would hardly further the policy

of Rule 56 to "eliminate a trial in cases where it is unnecessary and would only cause delay and expense." *Anthony v. Ryder Truck Lines, Inc.*, No. 79-1539, Slip op. at 7, 611 F.2d 944 at 947 (3d Cir. 1979), *quoting Goodman v. Mead Johnson & Co.*, 534 F.2d 566, 573 (3d Cir. 1976).

In determining whether the GAO's purpose in this case was authorized by the statutes, we must look to the source of the GAO's power to examine contractors' records. While the status of the GAO, as an agency of Congress, is not identical to that of administrative agencies of the executive branch, *see The Comptroller General's Authority to Examine the Private Business Records of Government Contractors*, 92 *Harv.L.Rev.* 1148 (1979), we find Professor Davis' principle of administrative law to be equally applicable to the issue of GAO's authority. That is, an agency's power to investigate can be exercised only for the purpose for which the authority was granted. 1 K. Davis, *Administrative Law* § 3.10. *See also Burlington Northern, Inc. v. Interstate Commerce Comm'n*, 149 U.S.App.D.C. 176, 462 F.2d 280 (D.C. Cir.), *cert. denied*, 409 U.S. 891, 93 S.Ct. 120, 34 L.Ed.2d 148 (1972); *Chattanooga Pharmaceutical Ass'n v. United States Dept. of Justice*, 358 F.2d 864 (6th Cir. 1966); *Shasta Minerals & Chemical Co. v. Securities & Exchange Comm'n*, 328 F.2d 285 (10th Cir. 1964); *Montship Lines, Ltd. v. Federal Maritime Board*, 111 U.S.App.D.C. 160, 295 F.2d 147 (D.C. Cir. 1961).

In determining for what purpose the GAO was granted authority to review business records of private businesses that contract with the government, we look first to the history of the access-to-records statutes. Congress in 1951 amended the Armed Services Procurement Act of 1949 and the Federal Property and Administrative Services Act of 1949 to require the inclusion in government contracts that are "negotiated without advertising" of provisions authorizing the Comptroller to audit and examine materials "directly pertinent" to the contracts. The remarks

of Representative Hardy, the sponsor of the amendment, make it clear that its purpose was to enable the GAO to determine whether suppliers of war materials under contracts let without competitive bidding were reaping excessive profits:

> In normal times, competitive bidding generally operates as a brake on the price which a contractor can demand from the Government for his goods and services. However, these are not normal times, and it should be obvious to all of us concerned with the expenditure of billions of dollars for national defense that we must establish every reasonable safeguard against waste and extravagance in the spending of these vast sums. Under conditions as they now exist, competitive bidding has little or no effect upon contracts which are negotiated without advertising. As a result, when a contract is being negotiated, here is a typical illustration of what usually happens: A contractor with years of experience comes to the conference table accompanied by an equally competent lawyer. The Government representative on the other side of the table will, in a great majority of cases, be at a tremendous disadvantage from the standpoint of both training and experience, no matter how conscientious and honest he may be. So, aside from any intentional liberality on the part of the Government contracting officer, there is every chance in the world that the Government will come out on the short end of the deal. The bill would at least enable the agent of the Congress to check the transaction both from the Government records and the contractors' books.
>
> The major purposes of the bill are twofold: One, to give the Comptroller General the proper tools to do the job the Congress has instructed him to do; and, two, to provide a deterrent to improprieties and wastefulness in the negotiation of contracts.

97 Cong.Rec. 13198 (October 15, 1951).

Before the current cases involving the pharmaceutical industry, there was only one judicial interpretation of the access-to-records provision of 10 U.S.C. § 2313(b), *Hewlett-Packard Company v. United States*, 385 F.2d 1013 (9th Cir. 1967). The Court there permitted the government to have access to production cost information, interpreting the statutory term "contract" broadly to include the general subject matter of the contract:

> In our opinion, however, the word "contract", as used in this statute is intended to have a broader meaning, embracing not only the specific terms and conditions of the agreement but also the general subject matter. The subject matter of these four contracts is the procurement of described property by the Government.
>
> Production costs directly pertain to that subject matter, because if out of line with the contract price, the contract may have been an inappropriate means of meeting this particular procurement need of the Government. While this appraisal could not affect these particular contracts, it could lead to the use of other methods of meeting future procurement needs. Production costs involve transactions relating to the contract, because they encompass business arrangements made by the contractor in obtaining the materials, labor, facilities and the like required by it in fulfilling its commitment with reference to the subject matter of the contract. *Id.*, at 1016.

We find that it is clear from the legislative history and from the interpretation of the *Hewlett-Packard* court that the statutory access-to-records provisions permit GAO to examine cost records of negotiated contracts[1] in order to

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[1] Plaintiff argues that the access-to-records provisions do not apply to negotiated contracts when the price is based upon a catalog price, as it was in this case. We disagree. The provisions, by their terms, apply to negotiated contracts without qualification. Moreover, the contract price in *Hewlett-Packard* was based upon listed catalog prices. 385 F.2d at 1014.

determine whether, as set forth in the legislative history, there have been "improprieties and wastefulness in the negotiation of contracts," or whether, as stated in *Hewlett-Packard*, the contractor's costs are "out of line with the contract price."

The uncontroverted factual record placed before the Court establishes that GAO seeks SmithKline's records for the cost-price comparison authorized by the statutes. The Court should look to the agency's own assertions of its reasons for seeking the information. *S.E.C. v. Chenery Corp.*, 322 U.S. 194, 196, 67 S.Ct. 1575, 91 L.Ed. 1995 (1947); *see also C.A.B. v. United Airlines, Inc.*, 542 F.2d 395, 402 (7th Cir. 1976). While the circumstances leading up to GAO's demand for access to SmithKline's records might suggest that GAO was seeking to gather information for an industry study for the enlightenment of Congress and the public, GAO's statements demonstrate that its purpose was to review the pricing of drugs supplied under specific government contracts. The Comptroller General's letter to SmithKline, quoted at length at p. 8, above, refers to a "review of the procurement of drugs by agencies of the Federal Government, including the pricing of drugs and pharmaceuticals procured under negotiated contracts," and "information as may be necessary for use to review the reasonableness of the contract prices and the adequacy of the protection afforded the Government's interests." The uncontradicted affidavit of Gregory Ahart further establishes that GAO seeks access to SmithKline's records for the purpose of reviewing pricing of drugs purchased by the government. Mr. Ahart stated: "GAO intends to use data obtained through the access-to-records clause contained in the specified contracts in a proposed review to determine the basis for the prices charged by the suppliers of the products procured by the Government under the specified contracts. . . ." (Ahart Aff. I ¶ 11). He further stated: "It is my opinion that the data . . . is necessary to review contract pricing by the Government's

suppliers of drug items in order to determine the adequacy of the protection afforded the Government by the negotiation techniques used by the procuring agencies." (*Id.* ¶ 12). While the government has stipulated [8] that it suspects no impropriety in pricing in connection with the specific contracts, nothing in the access-to-records statutes suggests that the GAO must suspect impropriety before it exercises its authority to review a contractor's records. We therefore conclude that GAO's demand for SmithKline's cost records was made for a purpose authorized by the statutes. Thus, on the basis of the record before this Court, it is not necessary for us to determine, as did the Seventh Circuit in *Eli Lilly, supra* that an industry-wide public information study is an authorized purpose for a GAO inquiry. *See* 574 F.2d at 910-12.

Having determined that the undisputed facts in this record show that the GAO's purpose was authorized by the statutes, we must now determine the permissible scope of GAO's access to SmithKline's records.

The government argues that its right of access extends to records of all costs which in some way affected the price of the drugs purchased under the contracts which are at issue. Specifically, the government demands access to records of materials, labor, overhead, distribution, research and development, and marketing costs, whether or not SmithKline's accounting system apportions these costs to individual drug products or contracts. SmithKline argues that such broad access is not authorized by the statutes, nor was it within the contemplation of the parties at the time the contract was signed.

The *Hewlett-Packard* case, *supra,* which held that the access-to-records statutes permitted the GAO to inspect

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[8] "GAO has no reason to believe that SmithKline made unreasonable or excessive profits with respect to the contracts which form the subject matter of this action." (Stipulation of the parties filed March 14, 1977).

all of a contractor's records of production costs of the item purchased under the contract, was decided well before any of the contracts here at issue was signed. While *Hewlett-Packard* did not define the meaning of "production costs" directly pertinent to the contract, the Seventh Circuit in *Eli Lilly* made it clear that, under the access-to-records statutes, the government is not limited in its inspection to the direct costs of manufacturing the drug covered by the contract. Such a limitation, in the drug industry, would defeat the purpose of the access-to-records statutes since, as the Court in *Eli Lilly* pointed out, manufacturing and distribution costs of drugs have been estimated to constitute as little as nine percent of the product's sale price. *See* T. Donald Rucker, *Public Policy Considerations and the Pricing of Prescription Drugs in the United States*, 4 International Journal of Health Services, No. 1, 1974, pp. 173, 174. We agree with Eli Lilly's reasoning that "the access-to-records clauses should be interpreted so that an item is 'directly pertinent' to a contract if it is a significant input in the price of the product purchased in the contract." 574 F.2d at 914-915. This Court concludes therefore that the access-to-records statutes, and the contract clauses based thereon, clearly permit the GAO to inspect the records of costs of materials, labor, overhead, distribution, research and development, and marketing and such other costs as are directly pertinent to the drugs for which the government contracted. Interpreting the access-to-records statutes in light of their purpose to permit a determination as to whether costs are "out of line with the contract price," it is clear that the GAO is entitled to inspect the records of all costs which go into the makeup of the price of the drug covered in the contract.

The Court will therefore order SmithKline to permit the GAO to inspect records of costs of material, labor, overhead, distribution, research and development and marketing and such other costs as are directly pertinent to the drugs purchased under the specified contracts. The Court

will include in its Order provisions concerning the confidentiality of records, as agreed by the parties.

Order

AND NOW, this 24th day of January, 1980, the Court, having considered the parties' cross-motions for summary judgment, having held a hearing thereon, for the reasons set forth in the Memorandum of this Court dated January 24, 1980, hereby ORDERS that plaintiff's motion for summary judgment is DENIED and defendant-intervenor's motion for summary judgment on its counterclaim is GRANTED as follows:

It is FURTHER ORDERED that the Comptroller General of the United States and his duly authorized representatives have the right to examine all books, documents, papers, or records directly relating to the pricing and cost of producing items furnished and cost of producing items furnished by plaintiff SmithKline under the following contracts numbered: V797P-5835(b), V797P-5892(b), DSA120-74-C-2519, DSA120-74-C-2518 and DSA 120-73-D-2968, including, but not limited to, records of experienced costs, including costs of materials, labor, overhead, distribution, research and development, and marketing, and such other costs as are directly pertinent to the drugs covered in the enumerated contracts;

It is FURTHER ORDERED that the plaintiff, SmithKline, its officers, agent, servants, attorneys, employees and all persons in active concert or participation with them who receive actual notice of an order by personal service or otherwise, are enjoined from preventing the duly authorized representatives of the Comptroller General of the United States from obtaining access to and examining such books, documents, papers, or records of the plaintiff that this Court has ordered the Comptroller General and his duly authorized representatives have the right to examine; and plaintiff SmithKline, including its officers and subordinates, are directed to have available on the premises

of SmithKline, and its other principal offices wherever located, such books and records upon reasonable notice by the Comptroller General or his authorized representatives;

It is FURTHER ORDERED that every book, report, papers, record, and other documents (all hereinafter referred to as "documents"), designated as confidential by SmithKline or any of its divisions or subsidiaries and provided or otherwise made available to the Comptroller General or any of his successors, agents, employees, or subordinates (all hereinafter referred to as "the Comptroller General"), and every summary thereof and extract therefrom, and all data and information contained therein, including accountants' work papers (all hereinafter referred to as "data"), shall be held in confidence and shall not be provided or otherwise made available by the Comptroller General to any person or agency outside the General Accounting Office except as provided in subparagraphs (a), (b), and (c), below. No copies of SmithKline's documents shall be included in accountants' work papers without the approval of SmithKline.

Any document and data referred to in the above paragraph shall be used by the Comptroller General solely for the purpose of a contract study. Upon completion of that study, the Comptroller General shall immediately return to SmithKline all documents described in that paragraph. Any data in which SmithKline, any of its divisions or subsidiaries, or any product manufactured or sold by any of them are or may be directly or indirectly identified which the Comptroller General deems it necessary to retain shall be retained by the General Accounting Office and deposited with and maintained by the Comptroller General under security measures to be agreed upon by the parties. Access to such data by any person shall be permitted only upon written authorization of the Comptroller General, and as limited in the subparagraphs following next denominated a, b, and c.

(a) Any of the data referred to in the above paragraphs may be published, provided to, or otherwise made available to a person or agency outside the General Accounting Office if the data are published, provided, or made available in such a way that any direct or indirect identification of SmithKline, any of its divisions or subsidiaries or any product manufactured or sold by any of them, is not reasonably possible. SmithKline shall be afforded a reasonable opportunity to examine and offer its comments regarding any data considered for release, including any report issued by the Comptroller General that includes such data, before release of the data or report.

(b) The Comptroller General may comply without regard to the limitations of this Order set forth above, with an official written request for any of the data referred to above submitted to him by either House of Congress, or any committee of the House of Representatives or the Senate, or any joint committee of the two Houses, having jurisdiction over the subject matter of the study referred to in the Affidavit of Gregory J. Ahart filed in this section, to the extent authorized and directed by law. The Comptroller General will cause prompt notice of any such request to be given to SmithKline and to this Court at least seven (7) calendar days prior to furnishing the data requested.

(c) The Comptroller General and the United States shall notify SmithKline promptly of any request for disclosure, subpoena *duces tecum,* civil action, or other order or application for an order seeking production, release, or disclosure of any data referred to above, and further agree to use their best efforts to protect the confidentiality of such data, except as provided above, including resort to appropriate judicial remedies and cooperation with SmithKline in such efforts.

Opposition

Office-Supreme Court, U.S.
FILED
JUN 9 1982
ALEXANDER L. STEVAS,
CLERK

No. 81-2082

IN THE
Supreme Court of the United States

OCTOBER TERM, 1981

CHARLES A. BOWSHER, COMPTROLLER GENERAL OF THE UNITED STATES, AND UNITED STATES OF AMERICA
Petitioners,

v.

SMITHKLINE CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR RESPONDENT

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PRESS OF BYRON S. ADAMS PRINTING, INC., WASHINGTON, D.C.

QUESTION PRESENTED

Whether the Comptroller General's authority to examine a contractor's records that are "directly pertinent" to a particular procurement contract includes authority to examine records of indirect costs unallocated to the products sold, merely because those costs are ultimately met by the contractor's general revenues, including payments under the procurement contract.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

No. 81-2082

CHARLES A. BOWSHER, COMPTROLLER GENERAL OF THE UNITED STATES, AND UNITED STATES OF AMERICA
Petitioners,

v.

SMITHKLINE CORPORATION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR RESPONDENT

Respondent SmithKline Corporation ("SmithKline")[1] does not oppose the granting of the petition for writ of certiorari filed in this case on behalf of the Comptroller

[1] SmithKline's non-wholly-owned subsidiaries and affiliates, set forth here in compliance with Rule 28.1, are Allergan S.A.; Allergan Canada; Allergan de Colombia S.A.; Allergan Ltd.; Allergan Productos Farmaceuticos Ltd.; Pharma-Allergan Vertrieb GmbH; Sauten-Allergan; Nelson Res. & Dev. Co.; Charles Rives Part.; Xonics Inc.; Branson Sonic Power S.A.; Edmonton Labs. Ltd.; Franklin Off. Assoc.; Franklin Partnership; Franklin Plaza Assoc.; Franklin Town Corp.; K.B.S.A.; Krautkramer Japan Co.; MedLab Holdings; Oak Internat'l Ltd.; SmithKline Instru. Co.; Walnut Ins. Co.; Wells-Krautkramer Ltd.; Branson Sonic Power Co. (S.A.) (Pty.); A. J. White Pty.; SK&F Labs, S.A.; SmithKline-RIT; SmithKline & French Canada Ltd.; Menley & James Ltd.; Surel Sutures; Laboratories SmithKline & French S.A.; SmithKline & French Laborator-

General and the United States. If certiorari is granted, however, SmithKline urges that its cross-petition also be granted and that the case be set for argument with *Bowsher* v. *Merck & Co., Inc.*, No. 81-1273 (cert. granted Apr. 19, 1982), and *Merck & Co., Inc.* v. *Bowsher*, No. 81-1472 (cert. granted Apr. 19, 1982).

STATEMENT

The court of appeals found that the General Accounting Office ("GAO") has sought access to SmithKline's confidential cost records because two Senators and their staff assistants wish to release those data publicly. Pet. App. 3a-4a. SmithKline and five other manufacturers were selected for this purpose because they had previously volunteered to assist GAO by providing information. *Id.*

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ies Ltd.; SmithKline & French Pension Trustees Ltd.; SmithKline & French Research Ltd.; Laboratories Gremy-Longuet; SmithKline Dauelsberg GmbH; Smith Kline & French Hellas S.A.; SK&F India; Chemico Pharmaceuticals; Smith Kline & French S.p.A.; Labs Julian de Mexico; Norden de Mexico; Smith Kline & French Nigeria; Smith Kline & French of Pakistan; Cainta Realty Corp.; SmithKline & Fujisawa K.K.; Fujisawa SmithKline Corp.; Smith Kline & French (Victoria Valley); Smith Kline & French Portgueso Productos Farmaceuticos; A. S. Ruffel (Private) Ltd.; Smith Kline Animal Health (S.W.A.) Ltd.; Smith Kline Antibioticos S.A.; Smith Kline & French (Switzerland) Ltd.; Smith Kline Dauelsberg Verwaltan GmbH; Smith Kline & French S.A.; Beckman Instruments Process-Gerate GmbH; Beckman Instruments Analytiques S.A.; Beckman Instruments International, S.A.; Beckman Instruments France S.A.; Beckman Instruments (Holding) Ltd.; Beckman Instruments Ltd.; Beckman Instruments (Nederland) B.V.; Beckman Instruments (Belgium) S.A.; Beckman - RJJC Limited; Beckman Instruments (Hong Kong) Ltd.; BICOMP, S.A. de C.V.; Beckman Instruments de Mexico, S.A. de C.V.; Beckman Instruments (Proprietary) Limited; Beckman (UK) Pension Trustees Limited; Beckman Instruments (Australia) Pty. Ltd.; Beckman Instruments Superannuation Pty. Ltd.

When the Senators would not be satisfied unless the manufacturers released detailed data without assurances of confidentiality, GAO issued statutory demands. *Id.*

GAO does not claim that SmithKline has made any excess or unfair profits, that any impropriety has occurred, or that there has been any violation of law. *Id.* at 5a. It selected the procurement contracts upon which its demand is based randomly among many similar contracts for the sale of items by SmithKline to the Government.

The court of appeals rejected GAO's sweeping interpretation of the statutes upon which it relies. It recognized that "the primary concern" of Congress in enacting those statutes was to permit access to records "in cases of suspected fraud and profiteering." *Id.* at 7a. It acknowledged that the legislative history "manifests a strong congressional intent to prevent unlimited 'snooping'." *Id.* at 20a. The court held that GAO's interpretation places "no doctrinal limitation" on its access powers, *id.* at 22a, and concluded that it "is inconsistent with the congressional intent and is entitled to no deference." *Id.* at 22a-23a.

Nonetheless, the court of appeals permitted GAO access to records of SmithKline's manufacturing costs, manufacturing overhead, royalty expenses, and delivery costs. It denied GAO access to records regarding costs of research and development, marketing and promotion, distribution and administration. *Id.* at 27a.

ARGUMENT

The court of appeals correctly decided the issue presented by the petition. In light of the specific and narrow purposes of the statutes upon which GAO relies, the court properly declined to authorize virtually limitless access by GAO to confidential cost documents that cannot be

"directly pertinent" to the non-cost-based procurement contracts upon which GAO's demand is based. Nonetheless, because the same issue is already before the Court in another case,[2] SmithKline does not oppose the granting of a writ of certiorari here.

If certiorari is granted, however, the appropriate course is not, as petitioners urge, merely to hold this case pending disposition of *Merck*. Fairness and sound judicial administration instead dictate two other steps. First, for reasons set forth in SmithKline's cross-petition for a writ of certiorari, filed simultaneously with this brief, the cross-petition should be granted so the entire matter may be before the Court. For similar reasons, such a cross-petition has already been granted in *Merck*. Second, this case should be set for argument with *Merck*.[3] For this purpose, SmithKline is prepared to meet any briefing schedule selected by the Court to avoid delay in the consideration of the two cases.

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[2] *Bowsher* v. *Merck & Co., Inc.*, No. 81-1273 (cert. granted Apr. 19, 1982; *Merck & Co., Inc.* v. *Bowsher*, No. 81-1472 (cert. granted Apr. 19, 1982).

[3] Ample authority for setting these cases for argument in tandem is provided by Rule 37 of the Court's Rules. *See also, e.g., Baxter* v. *Palmigiano* and *Enomoto* v. *Clutchette*, both reported at 421 U.S. 1010 (1975). *See generally* Stern & Gressman, *Supreme Court Practice* 752 n.30 (5th ed. 1978).

CONCLUSION

If the petition for a writ of certiorari is granted, the cross-petition should also be granted and the case set for argument with *Merck*.

Respectfully submitted,

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